January 31, 2001

Mr. Dale Gruen 01-8432.00
Portfolio Manager

SSR REALTY

1 California Street, Suite 1400

San Francisco, California 94111

SUBJECT: Market Feasibility Analysis of Multifamily Housing Development Opportunities at the Proposed "R Street" Project; Downtown Sacramento, California

Dear Mr. Gruen:

We are pleased to present our market feasibility analysis of the residential component of CalPERS' proposed R Street expansion project from 3rd to 7th Streets. Phasing of the subject project would logically be as follows: 1) construction of some 550,000 square feet of office and retail space and a residential component on the 4th Street Superblock site (3rd to 5th Streets between Q and R Streets), and 2) residential development on CalPERS' properties along R Street between 5th and 7th Streets.

Total residential floor area on CalPERS' properties fronting R Street between 3rd and 7th Streets is 180,000 square feet. Conceptually, residential development on the superblock would total between 60 and 80 units in a single-loaded, three- to four- story building.

This analysis primarily addresses demand, product pricing, and programming for rental apartment units. A secondary function of this analysis is to offer similar commentary, though of a preliminary nature, on for-sale housing. The report which follows summarizes our key conclusions and recommendations for the aforementioned residential component, as well as key market findings in support of the recommendations.

The objectives of this market analysis were to: 1) evaluate market demand and supply conditions and 2) produce conclusions on market depth, market positioning, and general product programming suitable for input into CalPERS' internal business planning.

To accomplish these objectives, we conducted the following analytical tasks: First, we evaluated the subject project's location as related to the Downtown Sacramento employment and living environment. Second, we evaluated Downtown employment trends to understand the size of the market that translates to potential renters and owners for the subject project. Third, we surveyed market rate apartments within Downtown Sacramento and nearby suburbs, considering project size, unit types and sizes, rental rates, features and amenities, and renter profile. Proposed Downtown apartment projects were also identified. A similar survey was carried-out for for-sale housing projects. Fourth, we prepared a statistical demand analysis to project the near-term market depth for market-rate apartments and for-sale housing in Downtown Sacramento, versus the existing and planned housing supply. Finally, we compiled analogue case studies of other Downtown CBDs with similar, emerging apartment living environments (Portland, San

Diego, Denver, and Dallas) as benchmark comparisons to the growing housing community of Downtown Sacramento.

KEY CONCLUSIONS

Our overriding conclusion is that the Downtown housing market is sufficiently deep to support residential development on both the Superblock and the CalPERS properties fronting along R Street between 5th and 7th Streets.

- We recommend rental housing for the superblock and for sale housing on one of the two R Street blocks, preferably the one between 6th and 7th Streets. The rental preference for the Superblock residential component reflects in large part a potentially challenging ownership structure created by the need for ground leasing. Recommended phasing would begin with the rental housing on the Superblock in order to establish the market, and then progress to the two R Street blocks.

  In short, the Downtown apartment market is strong, occupancies are high, and rents have increased significantly in the last year. Though nascent, the new construction for-sale market has shown tremendous strength with recent projects virtually pre-selling entirely.

- The recommended rental rates, value ratios and unit configurations shown below reflect the competitive positioning of the rental component of the project (i.e., newer construction, location, proximate land uses) relative to existing and proposed downtown apartment properties. (Exhibits I-1 and I-2). These rents assume 6- to 12-month leases, which are typical for Downtown area projects. Parking can be charged at $75 or more for subterranean spaces.

- The unit mix is based on our recommended unit distribution applied to total units. In the event that the final unit count for this project changes, the existing unit distribution can be applied to the new total. It is possible that a number of rental units may have to be set aside as "affordable" units. The number of affordable units will likely be determined through negotiations with the City or its representative organizations.

RECOMMENDED PRODUCT PROGRAM ASSUMING RENTAL HOUSING ONLY (180,000 SQ. FT.)

			AVERAGE	RECOMMENDED MONTHLY RENTAL RATES (1/2001)			
UNIT TYPE	UNIT MIX	% OF TOTAL	UNIT SIZE (S.F.)	RENT RANGE	RENT/SQ. FT.	AVERAGE RENT	RENT/ SQ. FT.
A Studio	48-54	30%	525	$845 - $920	$1.61 - $1.75	$880	$1.68
B 1B/1b	56-63	35%	750	$1,000 - $1,075	$1.33 - $1.43	$1,040	$1.39
C 2B/2b	56-63	35%	1,050	$1,250 - $1,325	$1.19 - $1.26	$1,290	$1.23
Total/Weighted Ave.	160-180	100%	788			$1,080	$1.37

- The majority of tenants are expected to be typically professional singles and couples who work in the Downtown CBD. Increasingly, empty nesters and retirees have become drawn to downtown Sacramento and also represent a significant market segment.

- Unit finishes should be comparable to newer suburban and downtown apartment projects (Exhibit IV-3) as more urban, avant-garde design is probably not yet suitable for this market.

- While data on lease-up history for downtown projects is unavailable, Adaggio, to the north of Downtown, leased at an average rate of 17 units per month. It is not unreasonable to assume that the subject property could average between 10 to 15 units per month during the initial lease-up period.

- The Fremont Building, located at 16th and P Streets, represents a rental housing product type for consideration along R Street east of 5th Street. The development density of this project is 78 units per acre.

- General for-sale housing price and size configuration information is shown below. Recommendations are based on the recently completed and proposed for-sale projects for which data is available in Downtown Sacramento. While the determination to build for-sale housing has not been made at this time, it should be noted that the parcels fronting R Street between 5th and 7th Streets represent a more suitable location for for-sale housing than does the CalPERS Superblock complex itself. In light of the recent success of detached for-sale product, townhome configurations appear to be the logical next step for the Downtown market (densities at 20 units per acre).

	UNIT TYPE	UNIT SIZE RANGE	AVERAGE UNIT SIZE (S.F.)	ESTIMATED BASE PRICE LOW	HIGH	AVERAGE	PRICE/ SQ. FT.
A	Townhome	1,100 - 1,500	1,300	$155,000	- $165,000	$160,000	$123
B	Flats	950 - 1,250	1,100	$135,000	- $145,000	$140,000	$127
C	Lofts	750 - 950	850	$125,000	- $135,000	$130,000	$153

As with rental housing, professional singles and couples, retirees and empty nesters represent primary market segments for this project. Unit finishes should be similar to those found in existing and proposed downtown projects although maturation of the for-sale market may present opportunities for more "urban" project design attributes (Exhibit I-8).

- The conclusion that the R Street corridor presents an opportunity to develop both rental and for-sale housing is evidenced by the estimated "surplus" (i.e., unmet demand) of downtown housing demand over existing and planned supply. As explained in the Downtown Housing Market Depth Section below, demand is generated primarily from Downtown employees, plus secondary demand from others relocating from within the greater Sacramento area (including retirees and empty nesters). The current unmet demand potential is estimated at about 600 market-rate rental units and 810 for-sale units. These numbers represent a base case scenario while an upper limit would place demand at up to 1,300 rental units and 1,200 for-sale units (Exhibit III-1).

The housing demand estimates and recommendations in this analysis assume that the local economy and housing market will continue at healthy levels for the near-term at least, with no *major* downturn or recession on the horizon. Several limiting conditions also pertain to this analysis. (See the "General Limiting Conditions" following this memorandum.)

The exhibits in the Appendix provide detailed housing market conclusions and recommendations, and the support data utilized in this analysis. The Appendix is organized into four sections: I. Recommended Market Positioning, II. Economic and Demographic, III. Demand IV. Rental, and V. For-Sale.

The balance of this report discusses in greater detail the issues and conclusions addressed above.

PROJECT DESCRIPTION

The project represents the residential component of the CalPERS headquarters expansion. This expansion will include some 550,000 square feet of office and ground floor commercial space at the superblock bounded by 3rd, 5th, Q and R Streets. The R Street corridor plan calls for a 3:1 office to residential ratio, which translates into another 180,000 square feet of residential area. In addition to the superblock site, CalPERS is considering residential development on the southern halves of the blocks bounded by 5th, 7th, Q and R streets for potential development.

CalPERS is currently pursuing acquiring additional land between 5th and 7th Streets in order to increase the marketability of the parcels that they currently own. Under consideration is the possible exchange of a parcel at 5th and Q Streets owned by CalPERS.

SUBJECT LOCATION

The subject project is at the southwestern edge of the CBD within the area designated as the "R Street Corridor." The subject site is just north of the well-established Southside neighborhood while Interstate 5 and the Sacramento River are located to the west.

Though on the edge of the CBD, the subject site is proximate to major office buildings (e.g., Lincoln Plaza, CalPERS) as well as existing residential areas (e.g., 200 P Street, Governor's Square, Southside). It is also part of the R Street Corridor area, the target of major revitalization efforts. The CalPERS headquarters expansion itself will be an important catalyst in this revitalization and provide an anchor for the area.

Regional access is excellent through proximity to I-5. Although conversations with City officials suggest that the light rail line will not extend to the site along R Street in the near future, the rail can be accessed a short distance from the site. Finally, third parties are working with the City to bring a chain supermarket to Downtown. This will further enhance the site and Downtown as a residential destination.

DOWNTOWN APARTMENT MARKET

Existing Downtown Projects

Downtown’s apartment market is maintaining very strong occupancy levels. Among the surveyed properties in the Downtown area (Governor’s Terrace, Capitol Towers, Governor’s Square, and Bridgeway Towers), occupancy rates linger just under 100%. This high occupancy indicates an undersupplied market. All of these projects are located within the CBD itself, with Governor’s Square just a few blocks from the subject site.

Market rate rents among primary competitors (listed above) range from $565 to $860 for studios, $860 to $985 for one-bedrooms, and $1,000 to $1255 for two-bedrooms (from base to maximum with premiums, and for 6- and 12-month leases). Typical value ratios among studios, one-bedrooms, and two-bedrooms range from about $1.15 to $1.60 per square foot per month. (The overall range is $0.94 to $1.62). These figures represent only typical floorplans and do not include penthouses, townhomes, or other configurations dissimilar to those found in the recommendations above. Typically, extra parking spaces are rented at $55 or more per month.

Renter profiles underscore the tenants’ connection to Downtown employment (Exhibit IV-3B). The majority of renters are young to middle-aged professionals who work in Downtown. However, most competitive Downtown projects are home to a number of retirees or empty nesters or suburban workers who also enjoy downtown living.

Given the improved economy and market over the past several years, Downtown apartment projects have seen tightening occupancies and rent escalations. Currently, occupancies are virtually at the highest levels possible (i.e., 98% - 99%). All of the competitive projects have seen rent increases over the last two years and, as a whole, average rents have increased nearly 9% since 1999 (Exhibits IV-8A and IV-8B). Also, the number of corporate tenants has diminished suggesting a more stable rental population.

Proposed Rental Projects

A number of new apartment projects and potential apartment development sites are in the “pipeline” in Downtown (Exhibit IV-9). However, it is not expected that they will total enough units to account for all of the estimated unmet demand in Downtown (as discussed in the Downtown Housing Market Depth section of this report).

Two of these projects, the Fremont Building and 18th and L are currently under construction. Together, these projects account for some 215 market-rate units and about 30 more subsidized units. The remaining projects, which comprise roughly 600 additional units are still in the planning phases or are otherwise faced with challenges to development (as explained in Exhibit IV-9).

Although rents for the two projects under construction have not been finalized, proforma rents escalated according to market-wide rent increases show rents from about $650 to $850 for studios, $981 to $1,130 for one-bedrooms, and $980 to $1,585 for two-bedrooms. Value ratios are higher than those of existing construction. These range from about $1.30 to $1.60 per square foot per month.

The recommended value ratios, ranging from about $1.23 to $1.68 per square foot per month, are well above those of existing Downtown projects and comparable to those planned and proposed for which data is available (Exhibit I-3). By comparison, the average value ratio for planned and proposed projects is about $1.32. However, recommended rents are lower than those of planned and proposed projects in absolute terms. This can be explained by the lower average unit size of the recommended rental product which is more in line with new product entering the market.

DOWNTOWN FOR-SALE MARKET

Existing Projects

Recent new construction for the for-sale market has been primarily comprised of small lot, detached product (Exhibit V-2). These projects have met with strong market acceptance as evidenced by the Metro Square and Capitol Park Homes project, which virtually pre-sold entirely. Smaller projects, such as Constantine Court and another at 13th and F, have enjoyed similar success.

Resale condo and townhome activity has likewise picked up in the last year and has been accompanied by price increases (Exhibit V-6). Among the three resale projects for which we gathered data, average price increases over the last year have been as high as 20% or more. For these projects, recent sale prices have started under $100,000 and reached an upper range of about $200,000.

Planned and Proposed Projects

Among planned and proposed for-sale projects are a number of condo and loft projects which represent some of the first attached product downtown in about 10 years. Most significant among these are the CADA Warehouse and 931 T Street projects which, by their performance, will evidence the demand for attached product downtown. They will also provide lessons on appropriate pricing, design and finish configurations as they are completed in Summer 2001.

For-sale housing development in the Downtown has been characterized by public financing participation either through land contribution or forgivable loans. As a result, starting prices for new attached projects are estimated to be in the low- to mid-$100,000s for small lofts or flats (Exhibit V-3). Townhome prices go as high as $207,000.

As mentioned before, parcels fronting R Street between 5th and 7th Streets present a suitable location for for-sale housing, with our preference for the block between 6th and 7th Streets.

ESTIMATED HOUSING MARKET DEPTH

While always a major employment center, Downtown Sacramento living has become increasingly popular in recent years. This can be attributed to a number of reasons including: national trends demonstrating greater interest in downtown living; proximity to employment centers, parks and entertainment retail; increased freeway congestion; affordability; and the ease of maintaining a smaller or attached home.

RCLCo conducted a structural demand analysis for market rate housing based on Downtown CBD employee households and estimated propensities to live in Downtown (Exhibit III-1). The analysis utilizes a Downtown Sacramento CBD employment base of about 109,000 employees (2005 estimate).

The 109,000 CBD employees are segmented first to account for those who live with persons who also work in Downtown, to arrive at an estimated 104,000 households represented by CBD employees. These households are then factored by renter propensity and qualified by income to arrive at 37,000 potential renter and 33,100 potential owner households. "Propensity to live Downtown" factors -- 7.5% for renter households and 5% for ownership households -- are then applied and adjusted upwards to estimate a potential "demand universe" made up of 2,800 renters and 1,700 owners. These figures account for demand coming from non-CBD employees (i.e., suburban workers, retirees, etc.). Propensities are based on those observed in the downtowns of other Western U.S. cities, which vary between about 6% to 10% (Exhibit III-2, III-3). These factors can be influenced by such factors as the development history, amenities, affordability, retail/grocery availability, and perception of each downtown.

Building on this approach, the analysis is as follows: 1) gross rental demand ranging from a low of 3,052 to a high of 3,758 units, and gross owner demand ranging from a low of 1,821 to a high of 2,242 units; 2) existing and planned market-rate housing units at 2,451 rental and 1,010 owner units (excludes CalPERS R Street Corridor Project); and 3) unmet low forecast demand of 600 apartments and 810 for-sale units over the next five years, and an unmet high forecast demand of 1,300 apartments and 1,200 for-sale units. It should be noted once again that the demand forecasts reflects a statistical relationship between Downtown employees and the potential demand universe as derived from relationships found in the other case study cities.

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We sincerely appreciate the opportunity to serve you on this engagement. This analysis was prepared by Robert J. Gardner, Managing Director, Devang Shah, Senior Associate, and John Lucero, Senior Associate.

Very truly yours,

ROBERT CHARLES LESSER & CO.

GENERAL LIMITING CONDITIONS

Every reasonable effort has been made to insure that the data contained in this study reflect the most accurate and timely information possible and it is believed to be reliable. This study is based on estimates, assumptions and other information developed by RCLCo from its independent research effort, general knowledge of the industry and consultations with the Client and its representatives. No responsibility is assumed for inaccuracies in reporting by the Client, its agent and representatives or any other data source used in preparing or presenting this study. This report is based on information that was current as of December 2000, and RCLCo has not undertaken any update of its research effort since such date.

Our report may contain prospective financial information, estimates or opinions that represent our view of reasonable expectations at a particular point in time, but such information, estimates or opinions are not offered as predictions or as assurances that a particular level of income or profit will be achieved, that events will occur or that a particular price will be offered or accepted. Actual results achieved during the period covered by our prospective financial analysis may vary from those described in our report and the variations may be material. Therefore, no warranty or representation is made by RCLCo that any of the projected values or results contained in this study will actually be achieved.

Possession of this study does not carry with it the right of publication thereof or to use the name of "Robert Charles Lesser & Co." or "RCLCo" in any manner without first obtaining the prior written consent of RCLCo. No abstracting, excerpting or summarization of this study may be made without first obtaining the prior written consent of RCLCo. This report is not to be used in conjunction with any public or private offering of securities or other similar purpose where it may be relied upon to any degree by any person other than the Client without first obtaining the prior written consent of RCLCo. This study may not be used for any purpose other than that for which it is prepared or for which prior written consent has first been obtained from RCLCo.